No. 80-1152

IN THE

Supreme Court of the United States

October Term, 1980

ROCHESTER GAS AND ELECTRIC CORPORATION,
Appellant,

v.

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Appellee.

ON APPEAL FROM THE COURT OF APPEALS OF THE STATE OF NEW YORK

MOTION TO DISMISS APPEAL OR AFFIRM JUDGMENT BELOW

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Appellee, pursuant to Rule 16 of the Rules of the Supreme Court of the United States, moves (1) that this appeal be dismissed on the ground that it does not present a substantial federal question or (2) that the judgment of the New York State Court of Appeals sought to be appealed from be affirmed.

Statement

This case involves an appeal from a determination (Appendix pp. 1a-2a)[1] of the Court of Appeals of the State of New York which upheld an order by appellee Public Service Commission of the State of New York (Commission) limiting the amount that may be included in rates chargeable to appellant Rochester Gas and Electric Corporation's (Rochester) ratepayers for institutional and informational advertising.

The Commission's order culminated its investigation of an application by Rochester for increased electric and gas revenues. The Commission, in a decision issued November 1, 1977 (Appendix pp. 42a-92a) granted Rochester $10 million in additional electric revenues and $2.5 million in additional gas revenues annually. In accordance with the usual policy, the rates authorized by the Commission were designed to yield the allowed rate of return during the first twelve months after the rates became effective.

As part of its rate determination, the Commission concluded that Rochester should be limited to an allowance of $^1/_{10}$ of one percent of gross revenues for institutional and informational advertising as prescribed by the Commission's Statement of Policy on Advertising and Promotional Practices of Public Utilities issued February 25, 1977 (Appendix pp. 173a-195a). Before issuing its Statement of Policy, the Commission had examined the institutional and informational advertising expenses of all New York State utilities. It concluded (Appendix pp. 184a-187a) that the advertising expenses were to some

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[1] References to Appendix _____ are to Appellant's Appendix to Jurisdictional Statement.

extent an inescapable cost of doing business but that ratepayers should not be forced to bear an unlimited amount of expenditures for this type of advertising. The Commission further found (Appendix p. 185a) that its staff spent far too much time examining expenses item-by-item to determine the amounts that should be includable in future rates and that its time should be employed in a more productive manner. Accordingly, the Commission announced its intention to allow a limited amount for institutional and informational advertising that would enable utilities to conduct advertising but would also be fair to the ratepayers (Appendix p. 186a):

> . . . On the basis of past practice, this allowance will, in all probability, range between $^1/_{10}$ and $^1/_{25}$ of one percent of operating revenues, in inverse relationship to the size of the companies. It will be determined individually for each company, in its next or pending rate case, [footnote omitted] on the basis of various other factors including size, geographical location, number of customers and costs of doing business in the area . .

The Commission in its opinion allowing increased rates for Rochester for the period starting November 1977 explained the application of its Statement of Policy to Rochester's advertising allowance (Appendix pp. 61a-63a):

> RG&E expended $755,082 during 1976 for advertising. This amount is well in excess of the range of reasonable advertising costs established in our Policy Statement on Advertising issued in February of this year. The lower and upper limits of that range for RG&E would be $122,200 and $308,000.

* * *

RG&E continues to argue for ratemaking recognition of the full amount of advertising expense that it incurred in 1976. It contends that the Policy Statement is unconstitutional and points to court decisions holding that managerial decisions are, in the absence of evidence to the contrary, presumed proper. RG&E fails to recognize, however, that it has the burden of proof in rate cases to establish that the expenses claimed are reasonable and representative of the level that will be incurred in the pertinent rate setting period. Except for a detailed description of how it spent $755,982 for advertising in 1976, RG&E has made no effort to prove that this level of expenditure is reasonable and necessary and representative of a reasonable amount of advertising for the period for which rates are being established. It is not enough to say, in effect, "this is what we spent and this is how we spent it." The company has an obligation and a burden to demonstrate why those amounts are reasonable, particularly in light of the fact that the company's advertising costs are well in excess of the guidelines set in our Policy Statement. RG&E has failed to satisfy its burden of proof and, therefore, we reject the company's contention that it is entitled to recover in rates set here the full amount of advertising expense it incurred in 1976.

It remains to be answered where within our guideline limits RG&E's allowance for advertising expense should be set. Staff argues for the lower limit but there is nothing to suggest that this is a proper result. In view of the company's extensive conservation and safety advertising programs, we will allow the upper limit of the range set in our guidelines even though RG&E's size and compact territory would argue for an amount closer to the middle of the range. The company also claimed a 6% per year allowance to cover escalation in advertising

> expenses from 1976. No inflation factor will be applied because we have selected an amount which we find to be a reasonable level of advertising expenses for the ratemaking year 1978.

The Commission reaffirmed its position on Rochester's advertising expenses when denying the company's petition for reconsideration (Appendix pp. 31a-41a). In response to Rochester's contention that a "presumption of regularity" existed with respect to historical expenses which had not been challenged, the Commission stated (Appendix, pp. 36a-37a):

> RG&E first complains that we have ignored the presumption of regularity which requires at least a *prima facie* rebuttal before a matter is put in issue and ignored what it describes as unchallenged evidence of the propriety of its test year level of advertising expense. We observed in our decision that the company's test year advertising costs were well in excess of the guideline limits set in our Policy Statement. Although RG&E repeatedly refers to the absence of evidence tending to rebut the propriety of its advertising expenditures, it chooses to ignore the testimony of two witnesses of intervenor Genesee Valley People's Power Coalition (GVPPC) that questions the need for the level of informational and institutional advertising incurred by the company,[1] as well as staff witness Rosenstrauch's adjustment deleting advertising costs in excess of one-twenty-fifth of 1% of operating revenues. Of course, the reason why staff did not examine the advertising expenditures of RG&E to ferret out specific disallowable programs and costs and why the particular items discussed by GVPPC were not evaluated was our announced decision to forego such

[1] One GVPPC witness questioned the need for specific RG&E advertising programs and advertisements as well as the overall level of advertising expenditures incurred by the company.

> unproductive, time consuming and costly review and to proceed by broadening the definition of the kinds of advertising we would allow without question, but to determine in each rate proceeding, a percentage of revenues constituting the maximum we would allow.

The Commission further discussed Rochester's failure to meet its burden of proof (Appendix p. 37a):

> RG&E also maintains that it satisfied its burden of proof as to the need for an advertising allowance equivalent to the amount it expended for that purpose in the test year. As we observed in our principal Opinion, however, RG&E's testimony on advertising is a litany of how and where it spent $755,982 on advertising in 1976 and concludes that an allowance within the Commission's Policy Statement range would be wholly inadequate. No effort was made to suggest why the test year level of expenditure was necessary and proper.

The Commission also rejected Rochester's argument that the Commission's limitation was an impermissible restriction on its freedom of speech (Appendix p. 37a):

> The company further contends that our decision interferes with its right to communicate with its customers and would require a reduction in desirable advertising programs. At the outset, it should be clearly understood that nothing in our Policy Statement or in our Opinion in this proceeding interferes with the company's right to communicate with its customers. Our action imposes a limit on the amount the company can recover from its ratepayers for that purpose; the company can spend more for advertising if it sees fit but the excess will be at the expense of the shareholders.

After its petition for rehearing was denied, Rochester commenced a proceeding pursuant to Article 78 of the New York Civil Practice Law and Rules to review the Commission's determination. The litigation concluded in a determination by the New York Court of Appeals affirming an order of the Appellate Division, Third Department upholding the Commission's decision (Appendix pp. 1a-2a).

In its memorandum-decision, the Court of Appeals considered Rochester's argument that it has a First Amendment right to have its ratepayers "... bear the expense of certain informational advertising which the Public Service Commission has found unnecessary to the functioning of utility services ..." The Court recognized that Rochester's expressional activity is entitled to First Amendment Protection citing this Court's decision in *Central Hudson Gas and Electric Corporation* v. *Public Service Commission*, _____ U.S. _____ (June 20, 1980). The Court of Appeals, however, rejected Rochester's First Amendment contention stating (Appendix pp. 1a-2a):

> ... But the Public Service Commission in this case has imposed no restraint, direct or indirect, upon petitioner's advertising or communications. Instead, the Commission has merely refused to include a portion of petitioner's information advertising as an allowable expense, and determined that such costs should be paid by the utility share-holders. ...

> It is an accepted principle that, although the Constitution may provide a citizen the right to engage in a certain activity free of governmental restrictions, it places no general corresponding duty upon government to ensure the availability of all resources necessary to realize that freedom (see, e.g., *Harris* v. *McRae*, 448 US _____, 48 USLW 4941, 4946-4947; *Norwood* v. *Harrison*, 413 US 455, 462). Thus, the Public Service Commission is not obliged to allow the utility to charge ratepayers for all communications which the utility may choose to make. On this view of the case, it is unnecessary to address the contention, made by the Commission, that inclusion of the entire cost of informational advertising as an allowable expense would violate the first amendment rights of ratepayers (cf *Abood* v. *Detroit Board of Education*, 431 US 209).

The Court of Appeals also rejected Rochester's challenge to the lack of evidentiary basis for the Commission's decision stating (Appendix p. 2a): ". . . [i]t cannot be said that this ruling is arbitrary, capricious or unsupported by substantial evidence [citation omitted]."

Rochester thereafter brought this appeal.

ARGUMENT

I. The Commission's decision is consistent with Rochester's freedom of speech.

Rochester contends (Jurisdictional Statement pp. 10-25) that the Commission's refusal to allow the utility to collect in future rates an amount equal to that spent in the past for institutional and informational advertising infringes on its right of free speech. Not only is the New York Court of Appeal's decision to the contrary correct, but Rochester also fails to raise a substantial constitutional claim.

The Commission's determination relates solely to how much money Rochester can charge its ratepayers for institutional and informational advertising. In the words of the Court of Appeals, the advertising in question is (Appendix p. 1a) "... unnecessary to furnishing of utility services ..." The advertising is under the control of utility management which may elect to spend as much as it desires or advertise in any manner it pleases. Here, there is no restriction on communication by the utility but merely an exercise of the Commission's ratemaking powers to assure that the ratepayers do not pay unnecessary or unreasonably high expenses for utility institutional and informational advertising.[2] The Commission, of course, has the authority and obligation under state law to allow only such rates as are just and reasonable (New York Public Service Law §66).

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[2] This case does not involve a prohibition or restriction on advertising as was the case in *Central Hudson Gas and Electric Corporation* v. *Public Service Commission*, _____ U.S. _____ (June 20, 1980) or *Consolidated Edison Company* v. *Public Service Commission*, _____ U.S. _____ (June 20, 1980).

The Commission's Statement of Policy (Appendix pp. 184a-187a) discusses the reasons why ratepayers should not be required to support unlimited amounts of institutional and informational advertising. While some of the advertising is obviously beneficial to consumers (*i.e.*, conservation measures, notification of emergency procedures, safety advice, etc.), there is a large middle ground of advertising that is neither clearly beneficial to consumers nor clearly political.[3] The middle ground consists, *inter alia*, of image polishing and attempts to create good will in the community it serves.

The Commission found (Appendix p. 185a) that it would be unproductive for parties in rate proceedings to examine and classify advertising voucher-by-voucher. Endless controversies would develop over relatively small dollar amounts. For ratemaking purposes the Commission concluded that the most practical way to proceed was to allow a pool of dollars to fund institutional and informational advertising. The application of the formula to the amount allowed Rochester is discussed in Point II.

Rochester attempts to take the Commission's ratemaking approach and elevate it to the level of a constitutional controversy. The simple truth is, however, that there is no authority to support Rochester's contention that a limitation on rates chargeable to utility customers violates its right to free speech.

Rochester concedes (Jurisdictional Statement p. 14) that "... the commission may limit its rate allowance for communication expenditures ..." but argues that this is a limitation on Rochester's free speech and therefore stan-

[3] No New York State utility is challenging the Commission's determination that the ratepayers should not pay for funding political advertising.

dards dictated by the First Amendment must be followed.[4] Rochester also appears to agree (Jurisdictional Statement p. 16) with the decision of the Court of Appeals (Appendix p. 2a) that even though the Constitution affords the right to engage in an activity, there is "... no general corresponding duty upon government to ensure the availability of all resources necessary to realize that freedom (see *e.g., Harris* v. *McRae,* 448 US _____, 48 USLW 4941, 4946-4947; *Norwood* v. *Harrison,* 413 US 455, 462) ...."

Rochester's sole rejoinder to that established principle is that the Court of Appeals failed to distinguish between affirmatively providing the resources and denying the opportunity to earn the resources. The purported distinction has no foundation in the law nor does it make sense, particularly in the context of utility ratemaking.

If the Commission had acceded to Rochester's request and allowed rates for its advertising program it would have forced the ratepayers (unless they chose not to use electricity or natural gas) to pay for the advertising in their rates. As the Court of Appeals observed, the result is no different from forcing taxpayers to fund abortions so that those who cannot afford them are not deprived of their rights (*Harris* v. *McRae, supra*). On the other hand, Rochester has not been deprived of the opportunity to engage in advertising and earn a fair return on its shareholders' investment. Advertising expenditures are within the discretion of management. Surely, if the utility spends more for image polishing than is allowed in rates, the shareholders may be forced to fund the program. But

[4] Rochester fails to explain how the Commission would have any authority at all to limit advertising costs to be paid for by ratepayers if this limitation is indeed one on free speech.

why should they not, if the advertising program is in excess of that found by the Commission to be beneficial to the utility's ratepayers who must pay the bills?[5]

A limitation on advertising expenses to be allowed in rates is no more a limitation on speech than any governmental restriction or program that lowers a company's earnings. Clearly, every tax could be subject to challenge on First Amendment grounds with the argument that the tax denied the company the opportunity to earn the resources needed to fund an advertising program.[6]

The Commission has done nothing more than require that any expenditures over the allowance be accounted for as "below-the-line" expenditures—not chargeable to the ratepayers. The constitutionality of treating advertising expenses as a below-the-line expense was litigated over a decade ago in *Southwestern Electric Power Co.* v. *F.P.C.*, 304 F.2d 29 (CA5), *certiorari denied sub nom. Alabama Power Co.* v. *F.P.C.*, 371 U.S. 924 (1962). In that case the United States Court of Appeals for the Fifth Circuit upheld a determination by the Federal Power Commission that expenses of advertising in favor of private power and in opposition to public power were

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[5] This Court has rejected the argument that persons can be compelled to subsidize the dissemination of views by others. *See, Abood* v. *Detroit Board of Education*, 431 U.S. 209 (1977), finding that union members cannot be compelled to subsidize the dissemination of views unrelated to the union's duties as exclusive bargaining representative. In the instant case, the Commission was concerned with advertising in excess of that needed to fulfill Rochester's public utility functions, but which absent the Commission's determination would have been supported by the ratepayers.

[6] Rochester's citation (Jurisdictional Statement p. 17) of *Murdock* v. *Pennsylvania*, 319 U.S. 105 (1943), and *Grosjean* v. *American Press Co.*, 297 U.S. 233 (1936), relating to taxation of free speech, is misplaced. Here there is no tax on Rochester's exercise of First Amendment rights but merely a refusal by the Commission to require the ratepayers to fund excessive advertising expenses.

to be categorized as political and thus most likely paid for by the stockholders rather than the consumers. The utilities in that case contended that classifying the expenses as political and thereby rendering them, at least presumptively, non-recoverable in rates, infringed on the utilities' right of free speech. The Court rejected that argument, stating (304 F.2d at 47):

> . . . We are unable to find here any basis for an argument of this character. As we have noted, nothing in the order prohibits or restrains the petitioners from publishing or republishing these or any other similar advertisements. Their freedom of speech or freedom of action in this area are not in any manner limited. All that has occurred in this proceeding relating to keeping of accounts is to exercise the Commission's discretion as to where these expenditures should be entered and to do so in such manner as to indicate the views of the Commission that such expenditures should not be subsidized by the consumers who purchase the power; that those expenditures should be charged to an income account [*i.e.*, the stockholders].

This Court has recently dismissed an appeal for want of a substantial federal question in a case similar to that presented by Rochester. *Laclede Gas Co.* v. *P.S.C.*, 49 U.S.L.W. 3492 (January 12, 1981). In that case the Missouri Commission had disallowed actual test year advertising expenses of $204,691, finding that the money was related to goodwill advertising. The state court concluded, 600 S.W.2d 222, 228 (Mo. Ct. of Appeals, Western District 1980):

> The evidence herein does not support Laclede's argument that the P.S.C. undertook the management of the company or that such action by the P.S.C. violated any constitutional right of Laclede to the exercise of its right of free speech.

The court found that the Missouri Commission could properly exclude advertising expenses which are not justified operational costs from the rates chargeable by the utility. In the instant case, as in Laclede, there is also no substantial federal question since the Commission has not intruded on Rochester's First Amendment rights.[7]

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[7] Rochester also argues (Jurisdictional Statement pp. 20-25) that since its First Amendment rights have been limited, the Commission faces a greater burden in disallowing advertising expenses than in disallowing other items for ratemaking purposes. Since Rochester has failed to show a limitation on its freedom of speech, its argument, which assumes a limitation, is without relevance. Needless to say, however, the Commission did follow lawful procedures when setting Rochester's rates, a matter discussed in Point II.

II. The Commission followed lawful procedures in determining Rochester's allowance for advertising expenses.

As a second argument, Rochester contends (Jurisdictional Statement pp. 25-31) that this Court should find a substantial Constitutional question arising from the manner in which the Commission decided to allow the utility less that it desired to spend for advertising expenses. Rochester would have this Court examine the ratemaking process and second-guess the findings of both the New York State Supreme Court, Appellate Division, Third Department (Appendix pp. 19a-29a) and the New York State Court of Appeals (Appendix pp. 1a-2a) as to procedures required under the New York State Public Service Law before the Commission may determine rates for a public utility. Of course, both the Appellate Division (Appendix pp. 25a-29a) and the Court of Appeals (Appendix p. 2a) found that the Commission complied with lawful procedures for purposes of judicial review in the State of New York; *i.e.*, the Commission's decision was not reversible under Article 78 of the Civil Practice Law and Rules on the grounds that it was arbitrary, capricious, unreasonable or unsupported by substantial evidence.

Rochester criticizes the quality of the evidence in its rate case before the Commission and it contends that the Commission improperly relied upon its Statement of Policy as a means of limiting the expense allowance for institutional and informational advertising. Contrary to Rochester's assertions, the Commission properly relied on the evidence before it, including its Statement of Policy, in deriving the rate award to be supported by the company's customers.

At the outset, it is important to understand that the expenses at issue are not "actual" expenses in any sense of the word. The complaint here is not that Rochester was deprived of recouping in the future expenses or capital outlays that it had actually incurred in the past. For this reason, *West Ohio Gas* v. *Public Utilities Commission of Ohio,* 294 U.S. 63 (1935) and *Missouri ex rel. Southwestern Bell Telephone Company* v. *Public Service Commission,* 262 U.S. 276 (1923), cited by Rochester (Jurisdictional Statement pp. 27-28), are not in point. Nor is this a case where the allowance for the future is lower than what the company will be required to spend. The presumption of reasonableness of past expenditures relied upon by Rochester (Jurisdictional Statement p. 28) is therefore not in point because the Commission has determined, after an investigation of expenditures by all New York State utilities, that a reasonable expenditure level for institutional and informational advertising in the future is less than Rochester spent in the past.[8]

Despite the clear statement of the Commission cited by Rochester (Jurisdictional Statement p. 29) that the Commission would determine an allowance for each utility in subsequent rate proceedings, taking into account the expenditure levels set in its Statement of Policy,

[8] *Pacific Gas and Electric Co.* v. *Federal Power Commission,* 506 F.2d 33 (D.C. Cir. 1974), cited by Rochester (Jurisdictional Statement pp. 28-29), has no bearing on this case. There, the Court was dealing with the question of whether an *ex parte* statement of policy issued by the Federal Power Commission was exempt from the rulemaking requirements of the federal Administrative Procedure Act. In the case of appellee Commission's Statement of Policy, all parties including Rochester were invited to submit comments which were reviewed by the Commission before the Statement of Policy was issued. The Commission specifically announced its intention (Appendix p. 186a) to rely upon the Statement of Policy in subsequent rate proceedings.

Rochester's evidence submitted to the Commission (Appendix pp. 217a-238a) utterly failed to justify an expense in excess of the range set by the Commission. Rather, it was only as the Commission noted (Appendix p. 63a), a statement of "... this is what we spent and this is how we spent it ..."

The Commission acted entirely reasonably in applying its Statement of Policy limitations to the allowance for advertising expenses claimed by Rochester. Rochester's claim that the Commission's decision is unreasonable and is not based upon substantial evidence fails, as the courts below determined, to raise a valid issue of state law let alone a substantial federal question.

Conclusion

For the above reasons, this appeal should be dismissed or the decision of the New York State Court of Appeals summarily affirmed.

Respectfully submitted,

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